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As I see it

HAS A MAJOR DEPRESSION STARTED?

FROM the middle of May through the first week in June the investors of America lowered their opinion of the value of American industry as indicated by the value of stocks listed on the New York Stock Exchange by about $5 billion. This is the biggest drop in the market since 1946, when values dropped about $15 billion in 40 days. The drop of 24% from the postwar peak of the market in 1946 to the present level cannot even remotely approach the drops from 1929 to 1932, when the Dow-Jones industrial average fell from $381.17 a share in September 1929, to $41.22 in July 1932, a drop of approximately 89%.

In Dewey and Dakin's book on cycles, they arrived at the opinion that the year 1953 is apt to be a very poor business year as at that time all of the various rhythms that seem to combine into the general business cycle, if these rhythms continue, will be heading down simultaneously. If 1953 is to be the worst year in the period ahead, it is quite possible that any recoveries between now and then will be very short and in each case will be followed by further and larger drops. A drastic depression doesn't develop overnight. From the stock market break in 1929 to the bottom of the depression in 1932 was a period of 2 years and 10 months. If 1953 is to be the bottom of another big depression, we could now be started on our way.

I think there might be a possibility that the stock market will go lower before a sustained recovery starts. There is no reason to believe, however, that the recent stock market behavior is indicating the beginning of another 1929. There are too many significant differences between the situation as it existed then and present business conditions to make it appear probable that the present business slide will grow to major depression proportions.

My reasons for believing that we are not entering a major depression at this time are as follows:

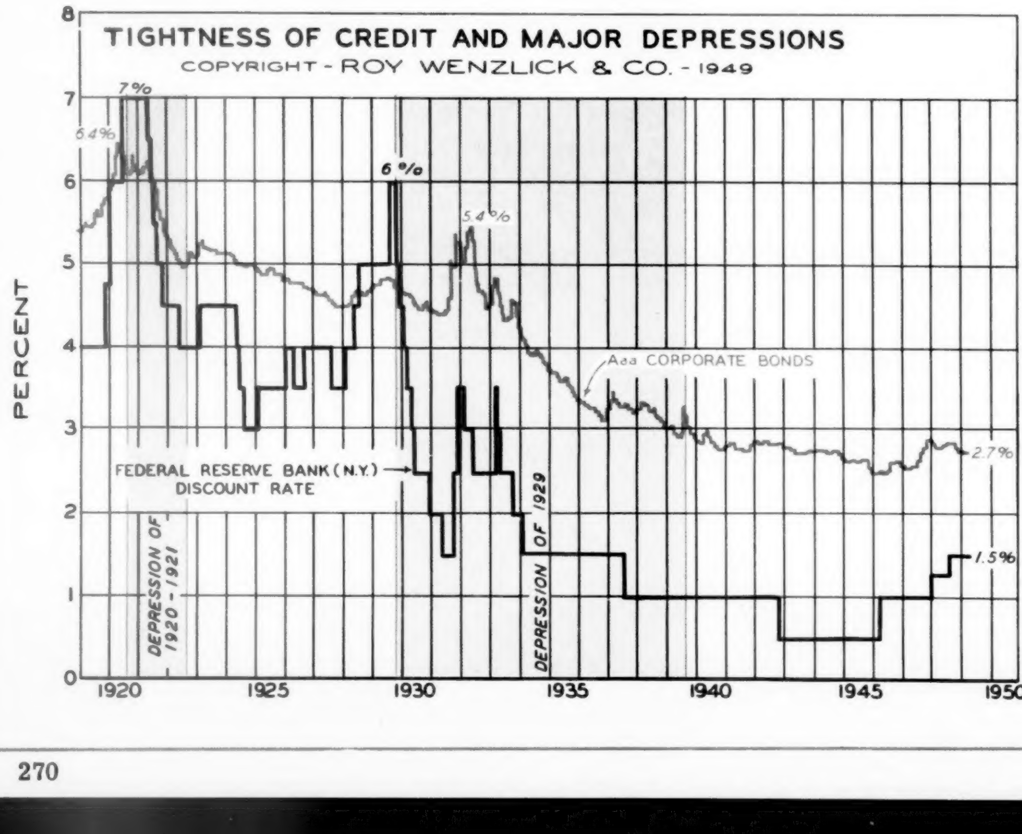
Every great depression in the past has been preceded by very tight credit. In 1920, just before the beginning of the depression of 1920 and 1921, the rediscount rate of the Federal Reserve reached 7%, and before the start of the 1929 collapse it reached 6% (see chart at the bottom of page 270). At the present time it is holding at 1.5%. Bank loans to business were at an average interest rate of 5.83 in 1929 and at present are running 2.70%. Interest yields on corporate bonds of the highest grade in 1920 reached 6.4%, while at the present time they are running 2.7%.

Brokers' loans on securities in 1929 averaged $6,563 million for the year; now they are running $350 million.

Business profits are still relatively high in comparison with their levels at the beginning of past depressions. In 1928 and 1929 we experienced a period long before the stock market break which was generally referred to as "profitless prosperity." Stocks in the latter part of 1929 were selling at 29 times earnings. Clearly, speculation had carried most investments to unsupported levels. At the present time, however, stocks are selling at 15 times earnings, indicating that relatively little inflation has affected the market.

Business failures at the present time, although they have increased during the past few months, are still on a very low level. This is the more surprising when it is remembered that in the postwar period many small, poorly financed and inexperienced operators started small businesses. It is my belief that eventually many of these marginal operators will be forced to close. In spite of this, however, business failures are running far less at the present time than they were in 1939, and certainly way below the high level of the late twenties.

In 1929, personal savings were almost nonexistent and personal credit was badly strained. Such personal savings as did exist were largely in stocks priced at fictitious values. Now, personal savings are very high, with cash and bank money held by individuals and business firms amounting to $165 billion, three times the volume of 1929. In addition, individuals hold $48 billion in savings bonds convertible into cash. In 1929, cash and bank deposits amounted to only $55 billion and



there were no savings bonds.

Insofar as the real estate and construction fields go, there are certain similarities and certain differences in relationship to 1929. At the time of the stock market collapse in 1929, real estate activity was only slightly lower than it is at the present time. It seems to me, however, that insofar as real estate went, the pattern of the boom of the twenties at that time was practically complete. While I do think that real estate activity will continue to decline during most of 1949 and probably during the initial portion of 1950, I would not be at all surprised to see a recovery in real estate activity develop which would bring it again above the normal line for a period of a few months, or even a few years. I am not at all certain that our present boom is entirely over.

Foreclosures, which in 1929 had risen to an average of approximately 30 per month per 100,000 families, are still hovering between 3 and 4. At the time of the stock market collapse in 1929 they had consistently been increasing for a period of 5 years. On the other hand, during the last 4 years, foreclosures have averaged lower than they have ever averaged at any 4-year period in the past. By this I do not mean that foreclosures will not increase in the period ahead; I think they will. Many mortgagees are starting to report, not foreclosures, but delinquent accounts, and undoubtedly some of these delinquent accounts will eventually become foreclosures. Until foreclosures climb month after month for a period of years, I will not be convinced that the real collapse is upon us.

Home mortgages now amount to about $33 billion. Of this, almost 1/3, or about $12 billion, is insured in some form or other by the Federal government. Farm mortgages in 1929 totaled an amount larger than the total of one year's farm income. Now, farm mortgage debt is running approximately one-fifth annual farm income. In 1929, the values of farm lands had been declining for a 9-year period. At the present time, farm lands as an average throughout the country have been declining for about a year. In 1929, approximately 6.6% of all residential dwelling units in urban areas in the United States were vacant, indicating a surplus of housing accommodations at that time. Today, a housing shortage still exists in most of the urban areas of the United States. While we think the housing shortage will disappear by the end of next year, it will be some time before residential vacancies reach the levels common during depression periods.

The peak of residential building volume in the United States was reached in 1925 and the rate at which we were building then in relationship to the number of families was far higher than any rate we have achieved in the postwar period. In the year 1925, we built 466 housing accommodations for each 10,000 families in the United States; in 1948, the peak thus far of our postwar housing boom, we built only 275 housing accommodations per 10,000 families. In 1929 we had passed the peak of our residential boom by 4 years; at the present time (if 1948 should prove to be the peak) we have passed it by but a single year. It is true that in 1929 we were in the midst of a tremendous building boom of office buildings, hotels and institutional buildings. This type of building boom has not yet occurred. It proverbially takes place at the tail end of each real estate boom. I have often said that when we start building big buildings in the United States, it is certainly time to run for cover. It is my opinion that we will not undergo so large a boom on this type of construction at the end of the present real estate boom as we did at the end of the twenties, but I am

confident that there is considerable building of this type still ahead of us before any major collapse occurs.

In 1929, office vacancy in the principal office buildings in the United States was running 10.5%. From this it climbed to almost 28% in 1934, due largely to the shrinkage of occupancy in existing buildings and to the completion of new buildings started in the latter twenties and the early thirties. At the present time, office building vacancy in the United States is averaging 1.6%, with relatively few new buildings being built.

The huge private debts of 1929 have been replaced by the huger government debts of the present. There is quite a difference, however, between private debt and government debt. Private debts can be called, forcing liquidation and contraction of operations. Public debt, especially in a country which is not on a convertible gold standard, can be expanded indefinitely, with the total destruction of the economy eventually, it is true, but without any sudden collapse. This probably makes public debt far more dangerous than private debt, but in considering the outlook for the next year or two I find nothing in the debt situation, either public or private, which would bring a total collapse.

I, therefore, feel confident that the present is not a 1929.

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